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BEFORE THE ARIZONA CORPORAT

COMMISSIONERS
BOB STUMP - Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

Arizona Corporation Commission

DOCKETED

MAY - 8 2013

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IN THE MATTER OF THE APPLICATION OF
SOUTHWESTERN TELEPHONE COMPANY FOR
A HEARING TO DETERMINE THE EARNINGS
OF THE COMPANY, THE FAIR VALUE OF THE
COMPANY FOR RATEMAKING PURPOSES,
AND TO INCREASE RESIDENTIAL RATES AS
NECESSARY TO COMPENSATE FOR THE RATE
IMPACTS OF THE FCC'S USF/ICC
TRANSFORMATION ORDER.

DOCKET NO. T-01072A-12-0472

DECISION NO. 73874

OPINION AND ORDER

DATE OF HEARING: March 25, 2013

PLACE OF HEARING: Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE: Teena Jibilian

APPEARANCES: Mr. Craig A. Marks, CRAIG A. MARKS, PLC, on behalf of Applicant; and

Ms. Maureen A. Scott, Senior Staff Counsel and Mr. Charles O. Hains, Staff Attorney, Legal Division on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On November 23, 2012, Southwestern Telephone Company ("Southwestern" or "Company") filed with the Arizona Corporation Commission ("Commission") the above-captioned application. The application states that it was filed pursuant to A.R.S. § 40-250 and Arizona Administrative Code R14-2-103, to compensate for the rate impacts of the Federal Communication Commission's ("FCC's") November 18, 2011 Universal Service Fund/Inter-carrier Compensation ("USF/ICC") Transformation Order ("USF/ICC Transformation Order").¹

* * * * *

¹ FCC 11-161, *Connect America Fund, WC Docket No. 10-90 et al., Report and Order and Further Notice of Proposed Rulemaking*, 26 FCC Rcd 17663 (November 18, 2011); *pets. for review pending* (10th Cir. filed Dec. 8, 2011).

1 customers in its Quartzite and Salome Exchanges. In its April 15, 2012, Utilities Annual Report,
2 Southwestern reported 1,986 residential lines and 924 business lines.

3 13. Southwestern is currently charging rates set by Commission Decision No. 63685 (May
4 24, 2001).

5 14. Southwestern is a rate of return incumbent local exchange carrier ("ILEC") eligible to
6 receive federal high-cost loop support ("FHCLS").

7 **FCC USF/ICC Order**

8 15. On November 18, 2011, the FCC issued the USF/ICC Order. The USF/ICC Order
9 provides for a transition from former federal universal service programs and most intercarrier
10 compensation systems into a new Connect America Fund ("CAF"). In its USF/ICC Order, the FCC
11 states that by July 1, 2020, intercarrier compensation rates for rate of return companies will be
12 reduced to zero. The recovery from the CAF will phase out over time at 5 percent annually.

13 16. The USF/ICC Order adds new rules that will reduce FHCLS to carriers by the amount
14 their flat-rate residential local service rates fall below a specified local service rate floor. The rate
15 floor includes state subscriber line charges, state universal service fees, and mandatory extended area
16 service charges, if any are assessed. The USF/ICC Order establishes those rate floors at \$14.00 as of
17 June 1, 2013, with the floor thereafter being determined annually by the FCC's Wireline Competition
18 Bureau.

19 17. As a recipient of FHCLS, Southwestern is affected by the FCC USF/ICC Order.
20 Under the USF/ICC Order, to continue receiving FHCLS, rural ILECs such as Southwestern must
21 increase their residential local rates to the FCC-mandated residential rate floors. Otherwise, the
22 amount of FHCLS funds received will be reduced dollar-for-dollar for each customer by the
23 difference between the existing local rate and the new rate floor.

24 **Application**

25 18. Southwestern's current rate for residential local service is \$11.25, and Southwestern
26 also serves two customers who currently have a grandfathered two-party line rate of \$9.60. The
27 application requests that Southwestern be authorized to raise all its residential local rates to the
28 \$14.00 rate floor mandated by the USF/ICC Order to allow it to continue receiving FHCLS.

1 19. Southwestern submitted the application, after consulting with Staff, in a “streamlined”
2 form. The application and accompanying exhibits in support of Southwestern’s requested increase in
3 residential rates are based on the twelve months ending June 30, 2012.

4 20. For the twelve months ending June 30, 2012, Southwestern’s filing indicates total
5 Intrastate Operating Revenues of \$1,646,758 (which includes FHCLS and Federal Safety Net
6 Additive Support of \$478,376), and total Intrastate Operating Expenses of \$1,746,502, for total
7 Intrastate Operating Income of negative \$99,744 before taxes, and negative \$60,315 after taxes.

8 21. The filing indicates a total Arizona rate base of \$4,138,383, of which \$1,572,768 is
9 interstate, and \$2,565,615 is intrastate.

10 **Staff Recommendations**

11 22. Staff states that it reviewed the application and the federal rule changes that prompted
12 its filing. Staff states that it concluded that the costs appear reasonable and appropriate under the
13 unique circumstances of this case, but that its recommendation should not be viewed as precedent for
14 the processing of future rate case applications.

15 23. Staff states that for the purposes of this proceeding, Southwestern stipulated to the use
16 of original cost less depreciation (“OCRB”) as the basis for a determination of its fair value rate base
17 (“FVRB”).

18 24. Staff reviewed and analyzed the filing, but did not perform a regulatory audit. Staff
19 does not recommend that Southwestern’s rates be set based on a revenue requirement analysis.

20 25. Staff states that the annual revenue effect of Southwestern’s requested increase in
21 local telephone service rates to \$14.00 would be \$53,368. Staff states that compared to
22 Southwestern’s total revenues, any revenue impact from this rate increase would be small, and any
23 impact on Southwestern’s fair value rate of return would be de minimus. Staff states that with
24 Southwestern’s requested increase, operating income would remain negative, and that the rate of
25 return would be less than zero, and not meaningful in this case.

26 26. Staff recommends that Southwestern’s monthly residence local exchange rate be
27 increased to \$14.00 to address the impact of the USF/ICC Transformation Order. Staff states that it
28 believes the requested increase is just, fair, and reasonable for the following reasons:

- 1 (a) The increase is necessitated by the FCC's November 18, 2011 USF/ICC
2 Transformation Order;
- 3 (b) The increase is necessary to preserve the entirety of the federal USF funds that
4 may flow to Southwestern pursuant to the FCC's rules;
- 5 (c) The increase will minimize/reduce the amount of future rate increase; and
- 6 (d) The increase will allow Southwestern to receive matching funds from the
7 FUSF.

8 27. The Staff Report states that on November 28, 2012, the Records Section of the
9 Corporations Division responded that Southwestern is in Good Standing, and a review of Consumer
10 Services database revealed that no complaints, inquiries and opinions were received pertaining to
11 Southwestern for the period January 1, 2009 – November 28, 2012.

12 28. Staff states that a check of the Utilities Division Compliance Section database showed
13 that Southwestern is in compliance with all items.

14 Conclusions

- 15 1. Under the particular circumstances of this proceeding, a rate of return analysis is not
16 useful.
- 17 2. According to the evidence presented, the rate increase request will have a de minimus
18 impact on Southwestern's return on FVRB.
- 19 3. Staff's recommendations are reasonable and should be adopted.
- 20 4. Under the particular circumstances of this proceeding, all Southwestern's rates for
21 residential local service should increase to \$14.00, and all other currently tariffed rates should remain
22 unchanged, in order to assure continued FUSF support for Southwestern's services.

23 CONCLUSIONS OF LAW

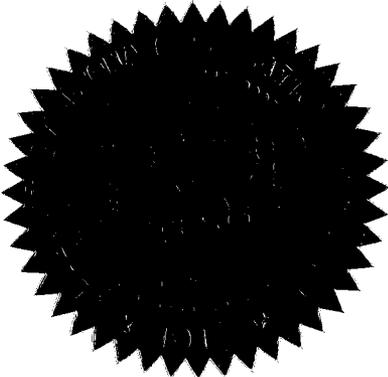
- 24 1. Southwestern is a public service corporation within the meaning of Article 15 of the
25 Arizona Constitution and A.R.S. §§ 40-250 and 40-251.
- 26 2. The Commission has jurisdiction over the Company and over the subject matter of this
27 proceeding.
- 28 3. The Company provided notice of this proceeding in accordance with law.
4. The Company's Arizona Intrastate FVRB as of June 30, 2012, is \$2,565,615.

1 IT IS FURTHER ORDERED that Southwestern Company is authorized and directed to file,
2 on or before May 31, 2013, revised schedules of rates and charges consistent with the Findings of
3 Fact and Conclusions of Law contained herein.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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8 *[Signature]* CHAIRMAN *[Signature]* COMMISSIONER
9 *[Signature]* COMMISSIONER *[Signature]* COMMISSIONER *[Signature]* COMMISSIONER
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11
12 IN WITNESS WHEREOF, I, JODI JERICH, Executive
13 Director of the Arizona Corporation Commission, have
14 hereunto set my hand and caused the official seal of the
15 Commission to be affixed at the Capitol, in the City of Phoenix,
16 this 8th day of May 2013.

17 *[Signature]*
18 JODI JERICH
19 EXECUTIVE DIRECTOR

20 DISSENT _____

21 DISSENT _____

1 SERVICE LIST FOR: SOUTHWESTERN TELEPHONE COMPANY

2 DOCKET NO.: T-01072A-12-0472

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